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FINANCIAL PERFORMANCE OF REGIONAL RURAL BANKS IN INDIA BEFORE AND AFTER AMALGAMATION

INTRODUCTION

The institute of Regional Rural Banks (RRBs) was created to meet the excess demand for institutional credit in the rural areas, particularly among the economically and socially marginalized section. Although the co-operative Banks and the commercial banks had reasonable records in terms of population group the co-operative banks had a clear urban bias. In order to provide access to low cost banking facilities to the poor, the Narshimhan working group (1975) proposed the establishment of a new set of banks as institution which "combine the local feel and the familiarity with rural problems which the co-operatives possess and the degree of business organization, ability to mobilize deposits, access to central money markets and modernized outlook which the commercial banks have".

Rural banking in India started since the establishment of banking sector in India. Rural Banks in those days mainly focused upon the agro sector. Regional Rural Banks in India penetrated every corner of the country and extended a helping hand in the growth process of the country. It was envisaged to combine desirable qualities of co-operative banks and commercial banks in RRBs, at the same time, it was emphasized that the role of RRBs would be to supplement and not supplant the other institutional agencies already existing in the field.

The Government of India promulgated the Regional Rural Banks ordinances on 26th September 1975, which was later replaced by the Regional Rural Bank Act 1976. The Preamble to the Act states the objective to develop rural economy by providing credit facilities for the development of agriculture trade, commerce industry and other productive activities in the rural areas, particularly to small and marginal farmers, agricultural labourers, artisans and small entrepreneurs.

The capital of RRB is contributed by the Union Government, concerned state Government and a sponsor bank in the ratio 50:15:35. From a modest beginning of 6 RRBs with 17 branches covering 12 districts in December 1975, the numbers have growth into 196 RRBs with 14446 branches working in 518 districts across the country in March 2005.

The RRBs have been in sharp focus over the last few years with several measures initiated towards strengthening them and making them vibrant channels of credit delivery, particularly for the rural sector. The most prominent of these has been the process of State wise amalgamation of RRBs sponsored by the same sponsor bank. Due to the process of amalgamation, the number of RRBs in the country declined from 196 to 96 at the end of March 2006 and further to 88 at the end of June 2008 and 84 at the end of March 2010.

LITERATURE REVIEW

Haslem (1968) revealed that the internal determinants originate from the balance sheets and the profit and loss accounts of the bank concerned and are often termed as micro or bank specific determinants of profitability. The external determinants are systematic forces that reflect the economic environment. The literature provides mixed evidence on the impact of liquidity on profitability.

Revell (1979) studied the relationship between bank profitability and inflation. He noted that the effect of inflation on bank profitability depends on whether bank wages and other operating expenses increased at a faster pace than inflation.

Chippa and Sagar (1981) discussed the variations in the level of banking development in Eighteen States in 1977 and studied its relationship with other social, economic and infrastructural variables. The analysis revealed that literacy rate followed by the infrastructural development emerged as the most dominant variables influencing the level of banking development.

Angadi (1983) measured the extent of concentration of priority sector advances in general and agriculture advances in particular in selected States in India. The analysis revealed that the degree of concentration of both priority sector advances and agricultural advances in the selected States had reduced in 1979 as compared to 1969-70.

Bhattacharya (1986) analysed the impact of branch expansion on the deposit mobilization in the different states of India. The broad conclusion drawn by the researcher was that all the four types of deposits were satisfactorily responsive to branch expansion in Maharashtra, Uttar Pradesh, Karnataka, Tamil Nadu, Andhra Pradesh, Gujarat, Punjab, Kerala and New Delhi. However in the states like Himachal Pradesh, Jammu & Kashmir, Assam, Orissa and Bihar, the

extent of branch expansion was very small in relation to the above mentioned states.

Kumar and others (1987) made an attempt to study the expansion of commercial banking facilities and extent of disparity in agriculture financed by the commercial banks in various states of India. The analysis revealed that the expansion of banking facilities had been extended more rapidly comparatively in rural areas as compared to Semi-Urban areas and Urban areas.

Bal Krishna and Sooden (1991) made an attempt to ascertain the extent of inter-state disparities with respect to commercial banking services in rural India during 1975 to 1985. The analysis suggested that the extent of disparities, with respect to all indicators of banking development except rural deposits per rural branch had come down in the year 1985 as compared to the year 1975.

Swami B. N. Anantha (2001) made comparative analysis of the performance of specific bank groups during 1996-2000 and concluded that the share in assets of scheduled commercial banks was declining in public sector banks and foreign banks while it was increasing in old private sector banks and new private sector banks.

Malhotra (2002) considered 22 different parameters that impacted the functioning of RRBs for the year 2000. Malhotra asserts that geographical location of RRBs is not the limiting factor for their performances. He further finds that it is the specific nourishment which was RRB receives from its sponsor banks which is cardinal to its performance.

Rao (2002) analyzed the impact of new technology on the banking sector-Technology changes the way business is done and opened new vistas for doing the same work differently in the most cost effective manner.

Sinha (2003) in a field study of 5 RRBs found that non-priority sector advances increased sharply in the second half of the 1990s for all the sample banks, of

which 4 banks have a significant 25 percent of their portfolio invested in non-priority sector loans.

Nitin and Thorat (2004) provide a penetrating analysis as to how constraints in the institutional dimension have seriously impaired the governance of the RRBs. They have argued that perverse institutional arrangements have given rise to incompatible incentive structures for key stake-holders such as political leaders' policy maker, Banks staff and elements have acted as constraints on their performance.

CHAPTER PLANNING

The study is divided into five chapters.

The first chapter is introductory in nature which covers development of banking in India, meaning and definition of banking, features of banking, and classification of banks.

The second chapter deals with RRBs. The following sub topics are included in this chapter like origin of RRBs, meaning of RRBs, capital structure of sponsors, management of RRBs, objectives, functions, progress and achievements of RRBs, difficulties faced by RRBs, role of sponsor Bank and amalgamation of Regional Rural Banks.

Research Methodology is dealth with in the third chapter. The following sub topics are included in this chapter: objectives of study, scope of the study, Hypothesis, sample selection, Data Collection, Tools and Techniques, limitations of the study.

The fourth chapter deals with financial peformances of RRBs in India before amalgamation and after amalgamation with the help of Ratio analysis, T-test, Anova and, Percentile.

The fifth chapter gives conclusions and suggestions based on data analysis.

RESEARCH METHODOLOGY

A. Research Statement

The following research statement is tested:

"Financial performance of Regional Rural Banks in India before and after Amalgamation"

B. Objectives of the Study

The objectives of the study are as follows:-

- To analyze the financial performance of Regional Rural Banks in India before and after amalgamation
- To understand the working of Regional Rural Banks in India

C. Hypothesis

- Null Hypothesis:

  The following null hypothesis is framed:

H_0: There is no significant difference in financial performance of RRBs in India after amalgamation.

- Alternative hypothesis:

  The alternative hypothesis is framed:

H_1: There is significant difference in financial performance of RRBs in India after amalgamation.

D. Scope of the study

The scope of present study is confined to Regional Rural Banks in India. The study mainly involves the financial performance of Regional Rural Banks in India before and after amalgamation. Similar studies on this line may be conducted for other banks in India and outside India.

E. Data Collection

The study is based on secondary data which is collected from secondary sources via-various journals, magazine, newspapers and annual reports and websites of regional rural banks and through various search engines.

F. Sample Size

For the present study, all the regional rural banks in India were taken for analysis. The process of amalgamation initiated in 2005, is now nearing completion. As a result of amalgamation process, the number of RRBs in the country declined from 196 to 96 at the end of March 2007 and further to 88 at the end of June 2008 and 84 as on January 2010

G. Tools and Techniques

The following tools and techniques are used for the present study

- Ratio analysis
- Percentage
- Mean
- Standard Deviation
- T-test
- Anova

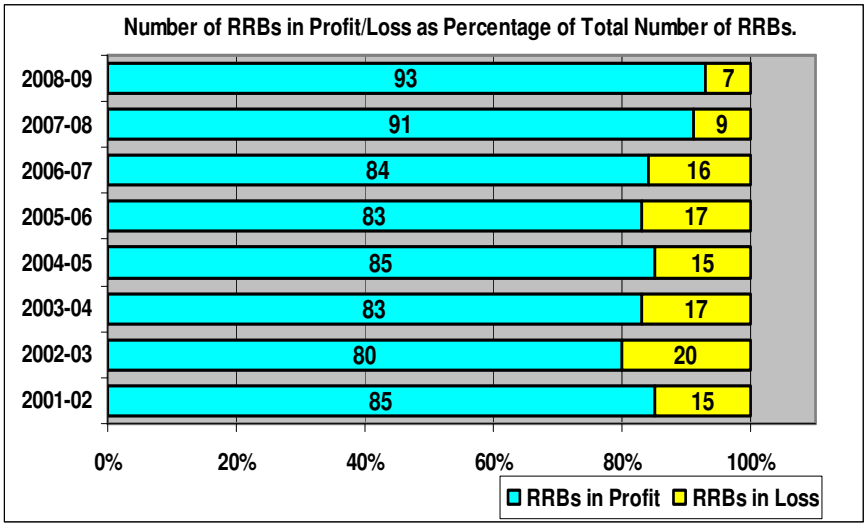
H. Limitations of the study

The present study is undertaken to maximize objectivity and minimize the errors. However, there are certain limitations of the study which are to be taken into consideration for the present work.

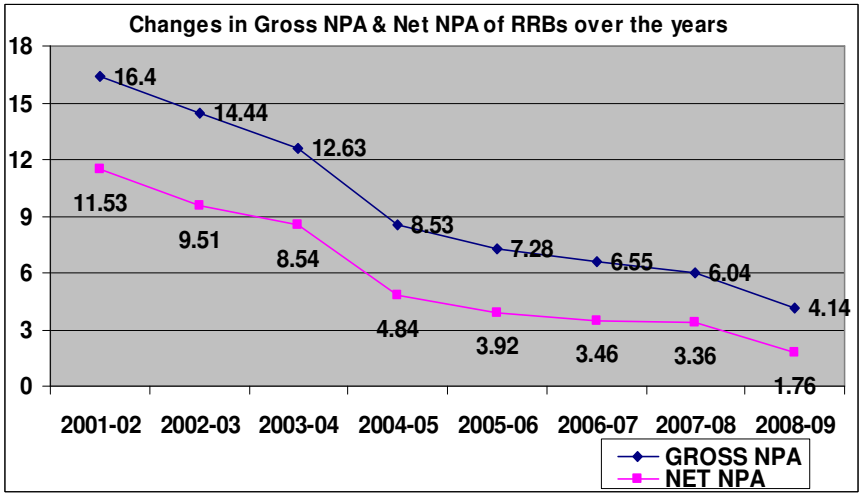
1. The study fully depends on financial data collected from the published financial statements of Banks.
2. This study incorporates all the limitations that are inherent in the financial statements.
3. Financial statements reflects the book value and the management might have window dressed or manipulated the values.

DATA ANALYSIS

- 15% of RRBs were loss making RRBs in 2001-02 but the numbers decreased to 7% in 2008-09. This proves that amalgamation has been beneficial to RRBs in reducing their losses.



- Also Net NPA of RRBs have reduced from 11.53% in 2001-02 to 4.84% in 2004-05 but after amalgamation the Net NPA's have further reduced from 3.92% to 1.76%. Thus amalgamation has been beneficial for RRBs to reduce their Net NPA.



- The Net worth of RRBs increased from 34% in 2001-02 to 56% in 2004-05. But after amalgamation the Net worth has further increased from 56% to 79%. This proves that amalgamation has helped RRBs in increasing their Net worth.

CONCLUSIONS AND SUGGESTIONS

RRBs are well positioned to play a major role in financial inclusion particularly in areas with high rates of financial exclusion. RRBs were originally created to cater to neglected sections as they were expected to have sound financial management combined with local feeling and familiarity.

RRBs should concentrate on asset quality and earnings. With the increasing competition among banks to meet customer expectations, banks should offer a broader range of deposits, Investments and credit products through diverse distribution channels including ATMs, telephone, internet.

The RRB staff are required locally and their postings or transfers are within the banks area of operation which is ordinarily a districts or two. The need for maintaining the local ethos makes it imperative that the emoluments and services conditions of the RRB staff should be inline with those of State Government staff in comparable cadres who constitute bulk of the salaried people in the area and with whom the former have to establish a close rapport for their day to day work. Therefore, the emoluments of the staff should be continued to be determined as per the state government scales. It is obvious that the terms of service and facilities available to the government staff may differ from state to state. However the terms and service conditions of the staff of RRBs operating within a state have to be uniform.

RRBs face many problems in finding suitable staff and in giving them adequate training. The sponsor banks are in a good position to assist RRBs in this

respect. The key personnel should continue to be provided by sponsor banks till RRBs are in a position to develop their own personnel through suitable training and otherwise to take over the relevant responsibilities. In this context, training of RRB personnel assumes great importance; while the SBI has set up separate training centres for the RRB staff, sponsor banks should conduct special courses for the RRB staff at centres meant for their staff. However, the existing arrangement cannot be said to be adequate. In States like U.P, Bihar, West Bengal etc. RRBs could not adhere to their branch expansion programmes for lack of adequate technical assistance in project formulation by RRBs. Facilities for recruitment and training and technical assistance should continue to be provided by the sponsor banks, on the same terms for a period of 10 years for each RRB. Thereafter, any arrangement of assistance of this type can be decided upon by mutual agreement between the sponsor bank and the RRB.

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